

December 31, 2019

Wade Crowfoot, Secretary
California Natural Resources Agency
1416 Ninth Street, Suite 1311
Sacramento, CA 95814

Dear Mr. Wade Crowfoot,

In accordance with the State Leadership Accountability Act (Leadership Accountability), the State Lands Commission submits this report on the review of our internal control and monitoring systems for the biennial period ending December 31, 2019.

Should you have any questions please contact Colin Connor, Assistant Executive Officer, at (916) 574-1800, colin.connor@slc.ca.gov.

GOVERNANCE

Mission and Strategic Plan

The Commission carries out its responsibilities in accordance with its Strategic Plan. The Commission's 2016-2020 Strategic Plan includes the following:

Vision Statement

The California State Lands Commission is a recognized leader that champions environmentally sustainable public land management and balanced resource protection for the benefit and enjoyment of all current and future generations of Californians.

Mission Statement

The California State Lands Commission provides the people of California with effective stewardship of the lands, waterways, and resources entrusted to its care through preservation, restoration, enhancement, responsible economic development, and the promotion of public access.

Strategic Goals

1. Lead innovative and responsible land and resource management;
2. Meet the challenges of the future;
3. Engage Californians to help safeguard their trust lands and resources; and
4. Cultivate operational excellence by integrating technology.

Commission staff operates under the direction of an Executive Officer who is appointed by the Commission. Staff is organized into eight divisions: Land Management, Mineral Resources Management, Marine Environmental Protection, Environmental Planning and Management, Legal, External Affairs, Information Services, and Administrative Services. As of fiscal year 2019-20, the Commission has 241 authorized positions and a budget of \$92.2 million.

The Commission's main program areas are:

1. Land and mineral leasing, including renewable and geothermal energy - The Commission issues leases for the use of the sovereign and school lands and development of the state's mineral interests under its jurisdiction. Leases may be issued for uses such as industrial wharves; commercial marinas; agriculture and grazing; bridges and utility rights of way; shoreline protective structures, public uses for recreation, restoration or wildlife refuge; private recreational docks, piers, and buoys; oil, gas, and mineral extraction; and wind, solar, and geothermal energy projects. The Commission currently manages approximately 4,000 leases.
2. Oil spill prevention - The Commission manages existing leases for offshore oil production facilities within three nautical miles of the coast, including oil-producing islands and offshore platforms. The Commission also regulates every marine oil terminal in California. Both functions form the Commission's oil spill prevention program, which is designed to provide the best achievable protection of public health, safety, and the environment and to prevent an oil spill in state waters. The Commission's prevention program has successfully limited the number and severity of oil spills in state waters. The Lempert-Keene-Seastrand Oil Spill Prevention and Response Act of 1990 covers all aspects of marine oil spill prevention and response and divides enforcement between the Commission and the Office of Spill Prevention and Response, a division of the Department of Fish and Wildlife. The Commission is responsible for the prevention aspects of the program.
3. Marine oil terminal engineering and maintenance standards - There are 34 marine oil terminals in California where nearly two million barrels of oil and petroleum products are transferred overwater (between ship and shore) daily. As an element of its oil spill prevention program, the Commission regulates all marine oil terminals in California, including enforcement of state building standards. Most marine oil terminals in California were built in the early 1900s when oil was carried by ships much smaller than the size of today's tankers, and before modern seismic safety standards and environmental requirements were established. The Marine Oil Terminal Engineering and Maintenance Standards, known as MOTEMS, are building standards (California Building Code, *Chapter 31F - Marine Oil Terminals*) that apply to all marine oil terminals in California. MOTEMS establish minimum engineering, inspection, and maintenance criteria for marine oil terminals to protect public health, safety and the environment, and govern the upgrade and design of terminals to ensure better resistance to earthquakes and reduce the potential of oil spills.
4. Marine invasive species program (MISP) - In coastal environments, commercial shipping is the most common vector for non-indigenous species (NIS) invasion. Ships are responsible for almost 80% of the NIS introductions to North America. Commercial ships transport organisms through two mechanisms: ballast water discharge and vessel hull biofouling. Commission staff board and inspect vessels to ensure compliance with ballast water management requirements by interviewing ship's officers and reviewing paperwork, including Ballast Water and Hull Husbandry Reporting Forms, ballast water management plans, and engine room logbooks. Staff also educates vessel crews about the requirements of California's Marine Invasive Species Act and distributes educational materials directly to vessels. The MISP is also active in

research and coordinates with the regulated shipping industry, other public agencies (state, federal, and international), leading scientists, and other stakeholders. Through these activities, the Commission has become a world leader in NIS management. The goal is to move the state expeditiously towards the elimination of the discharge of nonindigenous species into California waters.

Control Environment

The Commission establishes its control environment through multiple efforts.

The Commission's principles and values (shown below) are memorialized in its strategic plan and shape its culture while serving as a foundation upon which to achieve its mission in accordance with its vision.

- Accountability - Seek balance among competing uses with long-term protection of lands and resources.
- Integrity- Adhere to the highest ethical standards in all aspects of our work and service to the public.
- Engagement - Ensure robust and transparent public engagement.
- Quality - Provide superior public service through our expansive and unique professional staff expertise.
- Solution-oriented - Commit to making decisions in the public's best interest through collaboration, education, and use of the best science and technology.

At the organizational decision-making level, the three-member State Lands Commission oversees all programmatic activities transparently at public meetings conducted throughout the state approximately six times per year.

Levels of responsibility and authority are conveyed to staff through our Commission approved Delegation of Authority document and additional controls are documented through established policies and procedures. Additional expectations regarding staff conduct and responsibilities are communicated through division or work unit expectation memos.

The Human Resources Office routinely meets with the divisions to determine how best to assist in identifying their workforce needs surrounding hiring, developing staff, leadership succession and supporting performance and accountability management processes.

Information and Communication

The Commission collects information relevant to operational, programmatic and financial decision making through several avenues including its strategic planning process, budget change proposal process, contract request process, staff report review, and staff meetings at various levels throughout the Commission.

Because of its relatively small size, the Executive Office and senior management are generally aware of vulnerabilities and risks to the Commission. However, if staff at any level identifies what they believe to be a Commission-wide vulnerability, then that person can communicate that concern to their management. Management shall then confer with the Executive Office and if it is deemed that the concern represents a potential vulnerability, then the topic will be agendaized by that division for

discussion at a weekly senior staff meeting. The Executive Officer may determine that it is necessary to assign staff to study the issue and report back to senior staff or the Executive Office with recommendations to address the issue. If warranted, measures will be taken to respond to the vulnerability. Measures may include new written processes, practices, or procedures with a notification (email or memo) going to the affected staff. This process for communicating concerns or vulnerabilities was documented and shared with all staff in June of 2018.

Communication with external stakeholders is ongoing with updates on the Commission's activities and public meetings posted routinely on its website and through Twitter. In addition to web postings, the Commission actively engages with the community through Town Hall meetings, Environmental Justice Outreach meetings, project specific meetings and its public Commission meetings.

Employees who are aware of inefficiencies or inappropriate actions have several ways to report these to management or other entities. These options include discussing concerns directly with management, involving the Human Resources Office, Labor Relations Office or Equal Employment Opportunity Office, filing a whistleblower complaint with the State Auditor, or filing complaints with outside entities such as the Department of Fair Employment and Housing or the Equal Employment Opportunity Commission. Information on how to engage with these offices and outside entities is available to staff on the Commission's intranet site and/or on the displayed employment posters in each office.

MONITORING

The information included here discusses the entity-wide, continuous process to ensure internal control systems are working as intended. The role of the executive monitoring sponsor includes facilitating and verifying that the State Lands Commission monitoring practices are implemented and functioning. The responsibilities as the executive monitoring sponsor(s) have been given to:
Colin Connor, Assistant Executive Officer.

As the Executive Officer of State Lands Commission, Jennifer Lucchesi is responsible for the overall establishment and maintenance of the internal control and monitoring systems. She has assigned an executive monitoring sponsor whose responsibilities include facilitating and verifying that the State Lands Commission's internal control monitoring practices are implemented and functioning as intended. The responsibilities as the executive monitoring sponsor(s) have been given to Colin Connor, Assistant Executive Officer.

The Commission's Strategic Plan identifies its priority activities. The plan is developed with input from staff, management, Commissioners and key stakeholders and is subsequently monitored on an ongoing basis. Key staff members ("champions") from each division are responsible for each Strategic Plan action item. Staff's Strategic Plan activities are overseen by the Division Chiefs. The Assistant Executive Officer, with the assistance of an experienced staff person, monitors the progress of the Strategic Plan implementation on a regular basis. The Assistant Executive Officer provides updates to the Executive Officer. The Executive Office prepares an annual Strategic Plan update for the Commissioners. The annual update is a public document that is posted on the Commission's website. Executive staff presents the annual update to the Commissioners at a regularly scheduled public hearing near the end of the calendar year or at the beginning of the following calendar year. The annual update is used as an opportunity to review internal control processes and prioritize activities over the next year. Senior staff seeks input from all staff members on evaluating progress on Strategic Plan action items prior to publishing the annual update, and all staff is encouraged to review the completed

update.

In addition to the annual Strategic Plan update to the Commissioners, the Commission holds regularly scheduled public meetings approximately every two months. These meetings are an opportunity for the public to provide input to the Commissioners and staff on topics that may represent risks to the department. The meetings also allow the Commissioners to give direction to staff on how such matters should be addressed and monitored.

Throughout the year, the Commission's senior management staff holds weekly management meetings. Meeting topics include discussion of a wide range of current and potential internal control issues that need to be addressed, including Strategic Plan progress and issues related to the risks identified in this report. These meetings also allow management to elevate and discuss issues or vulnerabilities they or their staff have identified and decide what steps are needed to monitor or address the issues that arise.

Vulnerabilities may be identified by any level of staff up to senior management, including the Executive Office. Once identified, the issue is agendaized by that Division for discussion at a weekly senior staff meeting. The Executive Officer may determine that it is necessary to assign staff to study the issue and report back to senior staff or the Executive Office with recommendations to address the issue. The timeframe and manner for addressing the issue may vary depending on what is needed to correct it. This process was documented and shared with staff via a memo dated June 25, 2018.

Based on that decision, a new procedure may be put into place with a notification (email or memo) going to affected staff. The notification will detail who is responsible for monitoring the procedure and the timeline and the method of reporting to the Assistant Executive Officer.

Beyond internal methods to identify and monitor issues and vulnerabilities, the Commission engages with control agencies during external audits of various administrative and information technology functions. These audits serve as another avenue to identify and remedy any inefficiencies or vulnerabilities. Where deficiencies are found, ongoing reporting to the control entity may be required until remediation is complete.

RISK ASSESSMENT PROCESS

The following personnel were involved in the State Lands Commission risk assessment process: executive management, middle management, and front line management.

The following methods were used to identify risks: brainstorming meetings, employee engagement surveys, ongoing monitoring activities, audit/review results, other/prior risk assessments, and consideration of potential fraud.

The following criteria were used to rank risks: likelihood of occurrence, potential impact to mission/goals/objectives, timing of potential event, potential impact of remediation efforts, and tolerance level for the type of risk.

Risk Identification

The Commission updated and adopted its Strategic Plan in 2015. Through the strategic planning process, the Commission identified its vision, mission, guiding principles and values, and adopted strategic goals with strategies, key actions, and targeted outcomes. The Commission actively uses its

Strategic Plan to monitor progress and address risks to the agency that were identified as part of that process, and to ensure that the agency is adhering to its mission. Staff reports annually to the Commission on its progress in implementing its strategic goals.

The Commission's senior staff members, which include the Executive Officer, Assistant Executive Officer and division chiefs and assistant chiefs, meet weekly to identify and discuss issues, priorities, and risks to the agency. At these meetings, managers raise and discuss issues related to all aspects of the agency, including information technology and administration.

As part of the SLAA reporting process, a small team of staff, including the Executive Officer and Assistant Executive Officer, identified risks to the agency and then completed the risk identification process by aggregating the risks, including those raised during weekly management meetings, and the risks identified in the ongoing Strategic Plan process. The risks that were selected are those that may affect the Commission's ability to adhere to its Strategic Plan.

Risk Ranking

The team then ranked the risks based on their likelihood to occur, severity of impact, and how soon the impact could happen (velocity). Once the risks were identified and ranked, the team identified the controls in place to lessen or eliminate the risks and discussed the effectiveness of those controls.

RISKS AND CONTROLS

Risk: Key Person Dependence, Workforce Planning

As staff leaves the State Lands Commission, a gap in critical institutional knowledge and technical competence can occur unless careful workforce and succession planning, and knowledge transfer strategies are in place.

The Commission is a small entity with 241 authorized PYs in fiscal year 2019-20. As such, many of its staff have developed specialized and in-depth knowledge of certain programs or administrative areas that is not replicated in other staff members. The State Lands Commission has, over the last five to fifteen years and will continue, over the next five years to see numerous Baby Boomers retiring. This wave of retirement will include a large percentage of staff members with extensive program experience. As these vacancies are backfilled with the more mobile Gen X and Millennial staff, the Commission will continue to experience higher rates of staff turnover due to transfers and separations.

The Commission's 2016-2020 Strategic Plan recognizes Workforce and Succession Planning as a key action associated with the strategic goal of "Meeting the Challenges of Our Future." The Commission finalized its first Workforce Plan in 2018 and followed that up with its first Leadership Succession Plan in 2019. Implementation activities are currently underway. Unless properly implemented, a lack of workforce and succession planning combined with a dependence on key people could result in significant loss of institutional knowledge, decreased efficiency, and a decline in the Commission's ability to effectively execute its programmatic and administrative responsibilities as positions are vacated.

Control: Control A

The Commission's current Strategic Plan identified the need for workforce and succession

planning. In 2016, the Commission began the workforce planning process and subsequently committed to participating in a Workforce Planning Cohort offered by CalHR in 2018 which resulted in a completed Workforce Plan. This effort now requires focused engagement by human resources, management and senior staff to implement the included initiatives over the life of the plan. Implementation teams to address each initiative have been established. The Workforce Plan identifies areas where demographics suggest the Commission is most likely to lose staff and the gaps in knowledge that would be left by departing staff. To counter this, the Implementation Plan will develop strategies to enhance recruitment and retention and will develop needed training and knowledge transfer strategies during implementation.

Control: Control B

Upon completion of the Workforce Plan, the Commission embarked upon the development of its first Leadership Succession Plan. The 2019 Succession Plan focuses on strategies designed to develop potential leaders to ensure that leadership positions will remain filled with knowledgeable and competent leaders who can engage staff in meeting the Commission's strategic goals. Implementation activities are underway.

Control: Control C

The Commission has reduced the number and hours of working Retired Annuitants to reduce its reliance on key people who have already left the permanent workforce. This has forced programs to work with the Retired Annuitants and other staff to ensure that the institutional knowledge is being transferred to the permanent staff thus allowing them an opportunity to develop professionally. This reduction is also beneficial to the Commission's budget as it reduces its temporary help costs.

Risk: Recruitment, Retention, Staffing Levels

A major risk that can impact achievement of the State Lands Commission's strategic goals and objectives is the potential inability to quickly recruit and retain a skilled, trained workforce.

The Commission has experienced increased recruiting activity over the last five to ten years due to Baby Boomer retirements and anticipates a steady flow of retirements over the next five years as approximately 40% of its staff are currently age 55+. Transfers and separations of Generation X and Millennial staff members, who seem less content to stay with a single employer over a long period of time, have also been on the upswing. In addition to increased recruiting activity, the amount of staff time (both Human Resources and Supervisors) to conduct a recruitment has significantly increased since the State Personnel Board began conducting compliance audits approximately five years ago and making regulatory changes affecting recruitment. The Commission has doubled the number of PY engaged in recruiting activities yet has still identified another 2 PY of recruiting related work. These factors are amplified in recruitments for department-specific classifications which continue to be challenging due to the length of time and amount of staff time involved in conducting both examinations and recruitments.

Frequent turnover results in an increased vacancy rate, that combined with the length of time and number of hours involved in recruiting results in long periods of vacancy, reduced production, increased reliance upon key personnel, loss of institutional knowledge, and a negative impact to the succession

plan.

Control: Control A

The Human Resources Office is continuing to review its Hiring Process to identify any opportunities to decrease the amount of time involved in filling a division's request to fill a vacancy. Any identified efficiencies are incorporated into the process.

Control: Control B

The Human Resources Office has started to utilize more TAU (temporary authorization) appointments to fill positions where department specific examinations are required but no current list exists. A TAU appointment allows the Commission to recruit to fill the position before an examination is administered if the examination is subsequently administered within nine months of the appointment date. This reduces the timeframe to hire in these situations by three to six months.

Control: Control C

The Human Resources Office piloted its first Training and Experience, Continuous File examination in 2018. The use of Training and Experience exams is being expanded, where suitable, to other of the Commission's department specific classifications. Administration of these examinations would occur more frequently and have the potential to produce up-to-date lists with significantly less time and effort on the Commission's part to administer.

Risk: Litigation

The Commission can be sued in a quiet title action potentially resulting in loss of ownership to sovereign lands or school lands; loss of leasing revenue; tort liability resulting in monetary damages for failure to remove hazards to public health and safety or to the environment; for inverse condemnation and general takings claims; for statutory and regulatory compliance issues; various land use issues; toxics; water quality; and for failure to comply with the California Environmental Quality Act (CEQA) resulting in loss of lease revenue pending approval of an amended CEQA document. Similarly, the Commission engages in complex litigation including, but not limited to, Chapter 7 and 11 Bankruptcy cases; civil complaints against lessees for failure to pay rent; civil complaints against upland landowners who knowingly trespass on state-owned lands; condemnation actions against private landowners to ensure public access to sovereign lands; and numerous variants of torts cases that are undertaken to protect the interests of California, within the scope of the Commission's jurisdiction.

The Commission is charged by the Legislature with the management of the State's sovereign and school lands and resources. The most serious legal risks facing the Commission in its administration of these lands are: 1) challenges to the State's ownership due to the difficulty in locating the nature and extent of the State's sovereign land interest; 2) the failure of State lessees to meet their financial obligations (e.g., payment of rent, bond/security, environmental mitigation, restoration of lease premises); 3) challenges to environmental documents prepared by the Commission under CEQA; and 4) the failure to remove or mitigate human-made hazards on lands under the Commission's jurisdiction (e.g., leaking legacy oil wells; remnants of docks, piers, jetties, dams, and old oil production facilities; abandoned mines).

Depending on the cause of action, the State could lose valuable property and/or the State's general fund could incur hundreds of millions of dollars in litigation costs (to defend against or to pursue litigation), damages and settlement costs. Two recent bankruptcies of oil and gas lessees will cost the state over \$100 million to safely abandon offshore wells because of lessee insolvency. The more complex bankruptcy cases have also required outside counsel with specialized experience and who are admitted to practice in other states where the bankruptcies are filed.

Control: Control A

Litigation over the nature and extent of the State's sovereign interest is always present but managed by the coordination and support of the Commission's legal staff with its line divisions. The Commission provides its attorneys with extensive training regarding its jurisdiction and strives to resolve disagreements through settlements to reduce the threat of litigation.

Control: Control B

In recent years Commission staff have been reviewing the financial strength of its major lessees and their ability to meet their financial obligations. Whenever there is an opportunity to reopen a lease (e.g., assignment of lease, amendment, etc.), staff will renegotiate the terms to increase bond or surety or include other terms to reduce the financial and potential litigation risks to the state.

Control: Control C

The Commission reduces the potential for CEQA litigation by employing highly trained scientists and CEQA consultants and by providing review of the Commission's environmental documents by the Commission's legal staff. The Commission also, where appropriate, requires an applicant to indemnify the Commission and pay all litigation costs in the event of a legal challenge pursuant to CEQA or the Commission's action on the application.

Control: Control D

The Commission has a program to remove hazards from sovereign lands; however, the program activities are contingent on funding, which has been intermittent. Additionally, the Commission has also partnered for several years with the Abandoned Mine Unit of the Department of Conservation to remediate abandoned mines on state property thereby reducing the potential for personal injury to the public.

Risk: Funding - Sources, Levels

In upcoming years, several core programs and compliance activities will be impacted as the Marine Invasive Species Control Fund (MISCF) and the Oil Spill Prevention and Administration Fund (OSPAF) trend toward insolvency, due to internal and external overhead, statewide salary and benefit augmentations, and increasing operating costs. While this issue is not unique, the remedy is largely out of the Commission's control. The Commission is taking steps to mitigate the impact of these structural deficits and will continue to work with other impacted agencies to seek long-term solutions and preserve the fund balances.

MISCF, and by extension, the Marine Invasive Species Program (MISP) will be impacted by the federal Vessel Incidental Discharge Act (VIDA). Once fully implemented in December 2022, VIDA will preempt the state's authority across several program areas creating some uncertainty about MISP's future operations. Staff does not foresee issues with compliance; however, VIDA caps the fees that states can charge to inbound vessels reducing fee revenue to MISCF by up to \$500,000 per year (nearly 9% of the current annual fee revenue) starting January 1, 2023. At the same time, the Commission's growth places an increasing burden on the fund, as allocated overhead costs continue to creep, and staff salary and benefit costs continue to rise. Currently, MISCF bears around 10% of all Commission-wide allocated costs (with some variation), though this will likely need to be re-evaluated as the fund's balance declines. Based on current projections, MISCF will dip into the red by Fiscal Year 2024-25 without intervention.

OSPAF serves as one of the Commission's main funding sources for both the Mineral Resources Management Division (MRMD) and Marine Environmental Protection Division (MEPD), though fund administration rests with the Department of Fish and Wildlife's Office of Spill Prevention and Response (OSPR). The fund is facing a severe structural deficit, largely because fees have not kept pace with inflation and rising statewide costs (salaries, benefits, rents, etc.), and the fund balance will likely be depleted within the next three years if a fee increase is not approved. The Commission is working closely with OSPR to explore temporary options (e.g. expenditure cuts) and will be part of ongoing discussions around potential fee increases and other measures to address the structural imbalance.

Control: Control A

The Commission's priority is reducing all non-mission-critical expenditures to both MISCF and OSPA. This includes a deep review of prior year spending to identify any miscoded expenditures or misallocations that should have been borne by other funds, as well as carefully educating staff on the distinctions between the funds within the Commission's budget; this will build in additional controls and ensure that there are multiple opportunities to catch coding mistakes within any given procurement process.

The Commission's MISP staff is also exploring options to reduce spending and has already implemented limits on overtime and travel; if further reductions are necessary, staff will focus on first cutting internal research budgets (largely funding specialized research contracts with universities), which will limit the program's ability to adapt to and/or encourage new technologies in the field. Then, the program will look to reduce overhead costs, potentially revising how fees are collected to streamline administrative burden and other overhead costs. Staff would be the last to go, as the program is driven by their work; only at this point would the program face compliance issues, and this is not a likely scenario.

Control: Control B

In the near-term, the Commission will revisit its internal cost allocation practices to ensure that these two special funds are not bearing a disproportional share of Commission-wide expenses. Although it is common practice to allocate costs based on each fund's spending authority within the larger operational budget (minus any significant, one-time funding), the Commission recognizes that the status quo does not necessarily represent a best practice and sees an opportunity to better control costs at all levels. Upon completion of this internal review,

administrative staff will leverage FI\$Cal to automate the large majority of the cost allocation process and establish other controls to ensure that allocated expenditures are truly representative.

Control: Control C

In the long term, the Commission will explore opportunities to increase fee revenues and better manage expenditures to MISCF. One potential revenue stream is settlements from enforcement actions; however, over time, MISP strives for better enforcement and greater compliance by vessel operators, which means fewer revenue-generating judgements, so this is not a reliable revenue stream. The Commission also recognizes the opportunity to amend the Marine Invasive Species Act to place fees on different aspects of the MISP portfolio that are not directly governed or impacted by VIDA, including the biofouling management program and species monitoring program. All of these revenue streams are, however, very uncertain, so efforts will largely be focused on sustainable, long-term expenditure reductions.

With OSPAF, the future of the fund largely depends on the State's ability to adjust the fee to cover current and anticipated costs. The Commission expects to be heavily involved in these planning activities and will seek to contribute to a successful solution that avoids complete fund insolvency.

Risk: Internal Fi\$Cal Reporting

The July 2018 implementation of the new Fi\$Cal system at the Commission resulted in increased and unfamiliar workload and processes, which created difficulty in preparing timely and accurate reports to meet internal user needs. The Commission's Executive Office, Chief Administrative Officer, Budget Officer, and Program Managers rely on accurate and timely financial records to track and project revenue expenditures, budget status, fund balances, and make spending decisions. The learning curve and increased workload associated with Fi\$Cal resulted in a significant backlog in transactional entries. This in turn created a delay in the Accounting Office's ability to close each month's accounting books and run necessary reports.

Initially, staff had a lack of knowledge of how to work through the new Fi\$Cal processes. At this time, staff understands the processes and is tackling the backlog of transactions. Adding to the slowdown is the fact that Fi\$Cal and the State Controller's Office (SCO) are not keeping their books on the same platform and that the SCO has requirements that make it difficult for staff to accomplish reconciliations in Fi\$Cal. The Commission now must satisfy the requirements of two different systems, which requires significant additional time and effort.

While staff anticipates that these internal reporting issues will gradually be resolved as the backlog is eliminated, the Commission is currently (and has been for 18 months) experiencing a lack of certainty in its financial information, including final budget figures, fund condition information, and revenue figures. Staff is unable to reliably determine these data without a timely Plan of Financial Adjustment (PFA), which is derived from the currently delayed month-end closing process. The other financial reports run by staff and relied upon by decision makers are dependent on a completed PFA.

Control: Control A

To reduce the backlog of transactions, various accounting staff are working intermittent overtime.

Control: Control B

In the case of operational budget expenditures, budgeting staff are utilizing known contracts and assuming that the Commission will spend it to zero, then combining that information with known labor costs to estimate what may be leftover for non-baseline expenditures. This requires staff to err on the side of conservative decisions but prevents the overspending of appropriations.

Control: Control C

Where the Commission has received project-specific funding, staff is able to track these dollars off-line outside of Fi\$Cal in order to maintain reliable financial information.

Control: Control D

In the area of royalty reconciliation, staff is tracking these numbers through a spreadsheet so that our royalty accounting staff can perform reconciliations between their numbers and the Commission's accounting numbers.

Control: Control E

Commission management is evaluating how to organize the Fi\$Cal-related work and classify staff to ensure it has staff with the right skills in each position.

Risk: External Fi\$Cal Reporting

Much of the background information contained in the discussion of the "Reporting – Internal – Fi\$Cal Implementation, Maintenance or Functionality" risk also applies to this external risk.

In addition to the internal reporting issues, the implementation of Fi\$Cal in the 2018/19 fiscal year has created issues with generating accurate and timely external reporting. Specifically, the Commission is challenged by its current inability to close its books on time, on both a monthly and annual basis. This affects its ability to generate timely and accurate internal financial reports, which, in turn, impacts its ability to provide accurate financial reporting to the State Controller's Office and the Department of Finance. The Commission's annual School Lands Report to the Governor and Legislature and its annual Kapiloff Land Bank Report, which complies with the annual reporting requirement pursuant to Section 8618 of the Public Resources Code are difficult to prepare without current and accurate reports from Fi\$Cal and are therefore developed by relying on estimated financial information.

The Commission's inability to file timely Budgetary/Legal Year-End Financial Reports means that information provided to some outside entities is an estimate based on information derived from multiple internal financial records and not directly from official year-end filings. The State's credit rating in whole could ultimately be affected by late year-end reporting.

As mentioned in the "Reporting – Internal – Fi\$Cal Implementation, Maintenance or Functionality" risk, the Commission anticipates being able to resolve our reporting issues over time as the backlog of transactions is eliminated.

There is some overlap in controls between this risk and the "Reporting – Internal – Fi\$Cal Implementation, Maintenance or Functionality" risk.

Control: Control A

The budget staff is maintaining spreadsheets on revenue and special project funding outside of the Fi\$Cal system and uses this information to meet reporting requirements that cannot be fulfilled on time using Fi\$Cal reports.

Control: Control B

All revenue numbers are subject to an extra validation step before information can be released to the requesting external parties, including the Department of Finance. This involves intensive discussions between our most senior budgeting and accounting staff prior to release.

Control: Control C

The Commission is currently addressing the staffing shortfalls with temporary help until permanent resources are approved. This should accelerate the transactional catch-up process and ensure that future workload can be handled expeditiously.

Control: Control D

Commission staff is working closely with its Department of Finance's Fi\$Cal analyst to resolve problems related to reconciliations and the month- and year-end closing processes. The Fi\$Cal team assists with transactions as their time permits.

CONCLUSION

The State Lands Commission strives to reduce the risks inherent in our work and accepts the responsibility to continuously improve by addressing newly recognized risks and revising risk mitigation strategies as appropriate. I certify our internal control and monitoring systems are adequate to identify and address current and potential risks facing the organization.

Jennifer Lucchesi, Executive Officer

CC: California Legislature [Senate (2), Assembly (1)]
California State Auditor
California State Library
California State Controller
Director of California Department of Finance
Secretary of California Government Operations Agency